



FEDERAL ELECTION COMMISSION
Washington, DC 20463

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CERTIFIED MAIL
RETURN RECEIPT REQUESTED

ADVISORY OPINION 1993-23

Frederick K. Lowell
Pillsbury, Madison & Sutro
P.O. Box 7880
San Francisco, CA 94120

Dear Mr. Lowell:

This responds to your letter dated November 18, 1993, requesting an advisory opinion on behalf of Pacific Telesis Group ("PTG") concerning application of the Federal Election Campaign Act of 1971, as amended ("the Act"), and Commission regulations to the treatment of two separate segregated funds after a corporate reorganization.

PTG is a publicly-held corporation engaged in the telecommunications business. It was formed in 1984 following a Federal court-approved consent decree settling antitrust litigation against the American Telephone and Telegraph Company.^{1/} PacTel, also formed in 1984, is a wholly owned subsidiary of PTG and a holding company engaged in the wireless communications business through various subsidiaries and joint ventures.

PTG intends to "separate PacTel and create an independent publicly-held company," by a "Spin-off" of its stock in PacTel, i.e., by distributing its shares of PacTel to the shareholders of PTG. PTG proposes this separation for the following reasons: (1) to free PacTel from the MFJ; (2) to make it easier for the separate companies to obtain financing; and (3) to improve the conditions under which PTG and PacTel and their affiliates operate as a result of their common ownership - in particular, the affiliate transaction rules imposed by the California Public Utilities Commission.

PTG is the connected organization of Pacific Telesis Group Political Action Committee ("PTGPAC"). PTGPAC registered with the Commission as the separate segregated fund ("SSF") of Pacific Telephone on December 22, 1977, and was designated as the SSF of PTG on January

10, 1984. In anticipation of the Spin-off, PacTel established an SSF which filed its Statement of Organization on November 10, 1993 ("PACTELPAC"). You state that one of the reasons for this was "to assure continuing employees of PTG and employees of the soon-to-be-independent PacTel that their current contributions will not be used to further the political program of a corporation with which they will have no affiliation." PacTel intends to treat PACTELPAC as affiliated with PTGPAC until the Spin-off.

A. The Separation

The first step in the separation of PacTel from PTG was an initial public offering ("IPO") of 12-14 percent of PacTel's common stock which was expected to be completed early in December 1993.^{2/} The remaining 86-88 percent will be held by PTG, and, within six months from the completion of the IPO (approximately early June 1994), PTG will distribute the remaining PacTel stock to PTG shareholders ("the Spin-off")^{3/} on a pro rata basis, i.e., with the exception of certain options held by PTG directors, on a one-to-one basis.

In preparation for the IPO and Spin-off, PacTel amended its articles of incorporation and by-laws in October and September 1993 respectively. The S-1 states that certain provisions of these documents may have the effect of discouraging a tender offer or other takeover attempt. See S-1, pp. 84-85. These include a board of directors with staggered terms, prohibitions against shareholder actions by written consent, and the requirement of a 2/3 majority for amendments to the documents. PacTel has also adopted a shareholder rights plan, which you assert "may discourage unsolicited takeover attempts." You state that these provisions have been added to protect PacTel from "hostile takeovers," not to ensure continued control by PTG.

In April 1993, PTG elected three directors of PacTel (the entirety of its Board), all of whom are also PTG directors. At PacTel's first annual meeting of shareholders, which will take place by early February 1994, nine directors (including the three PTG directors) will be elected. Five will serve between early February and the Spin-off (the "Distribution Date"), and the other four will begin service on the Distribution Date. You assert that at least four, and probably five, of the nine directors will have had no previous employment or director relationship with PTG. In addition, at the time of the Spin-off, PacTel directors who are also directors or officers of PTG will resign from their PTG positions.

At the time of the Spin-off, certain employees of PTG will become employees of PacTel and certain PacTel employees will become PTG employees. You assert that, in no event, will any person be an employee or officer of both companies after the Spin-off.

As stated above, shareholders of PTG will own approximately 86-88 percent of PacTel's outstanding stock. This level of ownership is expected to change, however, as a result of subsequent trading of both PTG stock and PacTel stock. You indicate that no person or group, such as the officers and directors of PacTel, will hold dominant portions of PacTel stock. You explain that certain employee benefit plans sponsored by PTG will own stock in both entities, but the total percentage owned by such plans on the Distribution Date will not exceed 7.8 percent.

After the IPO, the relationship between PacTel and PTG will be governed by the Separation Agreement. This agreement provides that the separation of ownership of PTG and PacTel will be "total and complete" as of the Distribution Date. Separation Agreement, p. 7. It sets forth the operations of the two companies between the IPO and the Spin-off, and also thereafter. You assert that "[t]he clear purpose of this agreement is to divide the assets and liabilities of the companies, and to provide for the separate management of PTG and PacTel." For example, the Agreement provides that between the IPO and the Spin-off, PTG will be able to determine its future business opportunities, even if such determination excludes PacTel from business opportunities that would appear logical or beneficial for PacTel to pursue. (PacTel will, however, have an exclusive right to pursue cellular, paging, and radio location opportunities.) The Agreement further provides which agreements and arrangements will terminate on the Distribution Date, and which will continue. For example, the above-referenced agreement on business opportunities and contracts for general administrative services will terminate on the Distribution Date, while agreements for telecommunication services provided under tariff will not be terminated.^{4/}

B. Questions Presented

In view of the above-described Spin-off and surrounding circumstances, you ask the following questions: (1) Under the facts described, may PTGPAC and PACTELPAC be treated as disaffiliated as of the Distribution Date? (2) Once disaffiliated, will PACTELPAC be treated as a multicandidate committee? (3) Assuming disaffiliation of the PACs on the Distribution Date, may each disregard the other's pre- Distribution Date contributions for the purpose of compliance with the Act's contribution limitations?

C. Responses to the Questions

(1) The Act and Commission regulations provide that committees, including separate segregated funds, that are established, financed, maintained or controlled by the same corporation, person, or group of persons, including any parent, subsidiary, branch, division, department, or local unit thereof, are affiliated. Contributions made to or by such committees shall be considered to have been made to or by a single committee. 2 U.S.C. 441a(a)(5); 11 CFR 100.5(g)(2), 110.3(a)(1), and 110.3(a)(1)(ii). Under this rule, committees established by a single corporation and its subsidiaries are affiliated per se. 11 CFR 110.3(a)(2)(i). Advisory Opinion 1990-10.

Although PacTel will no longer be a subsidiary of PTG after the Distribution Date, Commission regulations also provide for an examination of various factors in the context of an overall relationship to determine whether one company is an affiliate of another and, hence, whether their respective SSFs are affiliated with each other. 11 CFR 100.5(g)(4)(i) and (ii)(A)-(J), and 110.3(a)(3)(i) and (ii)(A)-(J). The relevant factors are as follows: (A) the ownership by one sponsoring organization of a controlling interest in the voting stock or securities of another sponsoring organization; (B) the authority or ability of one sponsoring organization to participate in the governance of another sponsoring organization through provisions of constitutions, by-laws, contracts or other rules, or through formal or informal practices or procedures; (C) the authority or ability to hire, demote or otherwise control the decisionmakers of another sponsoring organization; (E) common or overlapping officers or employees, indicating a formal or ongoing

relationship between the sponsoring organizations; (F) members, officers, or employees of one sponsoring organization who were members, officers, or employees of another organization which indicates a formal or ongoing relationship or the creation of a successor entity; and (I) an active or significant role by one sponsoring organization in the formation of another. 11 CFR 110.3(a)(3)(ii)(A), (B), (C), (E), (F), and (I).

An application of these criteria indicates that the SSFs should no longer be considered as affiliated, effective on the Distribution Date. The Spin-off will end PTG's controlling interest in PacTel. Although the shareholders of one company (PTG) will comprise the large majority of shareholders of the other company (PacTel) immediately after the Spin-off, it is anticipated that PacTel and PTG shares will be traded vigorously on the open market leading to large numbers of different shareholders. In addition, it is expected that no single group of shareholders will hold a controlling interest in both corporations. See Advisory Opinion 1989-17.

Neither the Articles of Incorporation nor the By-laws of PacTel enable PTG to participate in its governance. The contracts, agreements, and arrangements that will continue after the Distribution Date as part of the Separation Agreement are considered "necessary and appropriate for [PacTel and PTG] to operate effectively after the Spin-off" (S-1, p. 80), but the governance and management of these companies is intended to be separate. In addition, after the Distribution Date, PTG and PacTel will not share any employees, officers, and directors. Thus, the factors set out in subsections (B), (C), and (E) are not present here.

With respect to subsection (F), the Commission notes that there will be PacTel personnel who, prior to the Distribution Date were PTG personnel (and potentially vice versa). Furthermore, PTG could be considered to have created the newly spun-off PacTel. In addition, there will be certain formal arrangements as part of the Separation Agreement. Nevertheless, these circumstances are outweighed by the Spin-off and Separation Agreement themselves which create a "competitive new publicly-held corporation" with entirely separate management. It is neither the subordinate of PTG nor its successor.

With respect to the factor set out in (I), the fact that PTG formed PacTel is superseded by the fact that PTG now proposes to sever the relationship between the companies and their respective SSFs.

The Commission believes that the situation you have presented is clearly distinguishable from the situations presented in two advisory opinions. In those opinions, the Commission declined to disaffiliate when a parent spun off a subsidiary in a tax-free reorganization, resulting in the end of the parent-subsidary relationship. Advisory Opinions 1987-21 and 1986-42.

In declining to disaffiliate the SSFs after the spin-offs in the above-cited opinions, the Commission relied on a number of factors. In both advisory opinions, the parent elected the board of the subsidiary before the spin-off and the subsidiary's by-laws made it difficult to take over the company or change the content of the board. In Advisory Opinion 1986-42, the parent elected all of the subsidiary's 12-member board and chose seven of its 14 directors to be on the board, thus giving the parent's directors majority control of the subsidiary's board after the spin-off.^{5/} In Advisory Opinion 1987-21, the parent elected the entire board of the subsidiary, and four

of the 12 directors of the parent's board were serving on the subsidiary's nine-member board after the spin-off. Although PTG, as majority shareholder after the IPO, will elect the nine-member PacTel board and PacTel by-laws make a takeover difficult, there will be no overlap on the boards of the two companies after the Spin-off; none of either company's directors will continue as directors of the other.^{6/}

In Advisory Opinion 1987-21, the Commission supported its conclusion by noting that "there exists significant overlap in the personnel and organizational structures of both corporations." As discussed above, there will be a complete separation of PacTel's group of directors, officers, and employees from that of PTG.

In both opinions, the Commission noted that immediately after the distribution date, all of the former subsidiary's stock would be owned by shareholders of the former parent. Here, however, the common identity of the shareholders will be broken with the IPO.^{7/}

Based on the foregoing, the Commission concludes that PTGPAC and PACTELPAC may be treated as disaffiliated as of the Distribution Date.

(2) Under the Act and Commission regulations, a multicandidate political committee is a political committee which has been registered for not less than six months, which has received contributions from more than 50 persons, and which (except for any State political party organization) has made contributions to five or more Federal candidates. 2 U.S.C. 441a(a)(4); 11 CFR 100.5(e)(3). Contributions by a multicandidate committee are subject to the limits of 2 U.S.C. 441a(a)(2), rather than 441a(a)(1), thus enabling it to contribute \$5,000, rather than \$1,000, to a Federal candidate with respect to an election.^{8/}

In prior opinions, the Commission has concluded that, since all affiliated political committees share a single contribution limit and may make unlimited transfers among themselves, a newly created political committee that becomes affiliated with a pre-existing multicandidate committee qualifies for treatment as a multicandidate committee. Advisory Opinions 1990-16, 1986-42 and 1983-19. In addition, the Commission has permitted two affiliated political committees to rely on the contributions made and received by either one, along with the period of FEC registration of the older committee, to achieve multicandidate committee status. Advisory Opinion 1980-40. The Commission concludes that PACTELPAC, having already qualified for treatment as a multicandidate committee through its affiliation with PTGPAC, will continue to be a multicandidate committee after the Spin-off.

(3) The Commission concludes that, after disaffiliation, the two SSFs may not disregard the other's pre-Distribution Date contributions for the purpose of complying with the Act's contribution limitations. As affiliated committees, they shared one set of contribution limits. In determining the amounts that each SSF may contribute to the same candidate after the Distribution Date, the committees must add the amounts given for a particular election by each of them before the disaffiliation and subtract that amount from the limit. For example, if before the Distribution Date PTGPAC gave \$2,000 (whether before or after the formation of PACTELPAC) to Candidate X for a 1994 House primary, and PACTELPAC gave \$1,000 to X for the same election, it would follow that, after the disaffiliation, the two SSFs may each

contribute \$2,000 to X for the same election. This result stems from the required attribution of a combined \$3,000 contribution to both SSFs as a consequence of their affiliation. Post-disaffiliation contributions by each committee to the same candidate would only be attributed to the committee making the contribution. Compare Advisory Opinion 1985-27.

This response constitutes an advisory opinion concerning application of the Act, or regulations prescribed by the Commission, to the specific transaction or activity set forth in your request. See 2 U.S.C. 437f.

For the Commission,

(signed)

Joan D. Aikens
Commissioner

Enclosures (AOs 1990-16, 1990-10, 1989-17, 1987-21, 1986-42, 1985-27, 1983-19, and 1980-40)

ENDNOTES

1/ This consent decree, known as the Modification of Final Judgment ("MFJ"), prohibits regional telephone companies and their affiliates from providing voice and data services beyond regional boundaries and restricts the lines of business in which such companies could engage, e.g. such companies may not design or develop telecommunications equipment or cellular phones.

2/ On August 27, 1993, PacTel filed a Form S-1 with the Securities and Exchange Commission ("SEC") registering the shares to be sold in the IPO.

3/ PTG has already received a ruling from the Internal Revenue Service that the Spin-off will qualify as a tax-free distribution under 26 U.S.C. 355.

4/ Arrangements for the allocation of intellectual property include the discontinuance by PacTel of the "PacTel" name after the earlier of PacTel's adoption of a new name or the second anniversary of the Spin-off. S-1, p. 82.

5/ Although all but one of the employees of the former parent and subsidiary companies resigned from each other's boards or as officers of the other, the board overlap of seven remained. (The remaining employee was, at the time of the opinion, president and CEO of the former subsidiary and served on both boards.)

6/ Although information directly related to this point is not discussed in Advisory Opinions 1987-21 and 1986-42, the Commission notes that four and perhaps five of the PacTel directors will have no prior relationship with PTG at the time of their election.

7/ Advisory Opinion 1987-21 also noted the requirement under IRS Reg. 1.355-2(c) that the shareholders of the parent have a "substantial continuity of interest" in the subsidiary after the distribution date. This continuity of interest would be satisfied unless pursuant to a pre-distribution plan or intent, the parent's shareholders were to sell or otherwise dispose of more than 50 percent of the parent's or subsidiary's stock. Although the companies' compliance with this tax provision to achieve a tax-free spin-off is suggestive that some continuing relationship exists, an analysis of the criteria for affiliation as presented in Commission regulations and previous Commission opinions indicates that the disaffiliating factors are of greater significance than the "continuity of interest."

8/ Multicandidate committee status, however, limits the committee's contributions to a national party committee to \$15,000 in a calendar year, rather than \$20,000.